SUPREME COURT, U. S.

JUN 20 1967

JOHN F. DAVIS, CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1967

No. 269

SOLITE CORPORATION
Petitioner

v.

UNITED STATES OF AMERICA
Respondent

PETITION OF SOLITE CORPORATION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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Printed by TEAGLE & LITTLE, INC., Norfolk, Va.

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Petitioner prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Fourth Circuit entered in the above styled case on March 30, 1967.

OPINIONS BELOW

The opinion of the United States District Court for the Eastern District of Virginia, Norfolk Division, Walter E. Hoffman, Chief Judge, a copy of which is attached as Appendix A, is reported at 254 F. Supp. 147 (1966).

A copy of the opinion of the United States Court of Appeals for the Fourth Circuit, which has not yet been reported, is attached hereto as Appendix B.

JURISDICTION TO REVIEW

The date of the judgment of the Court of Appeals sought to be reviewed is March 30, 1967. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

QUESTION PRESENTED

Whether, as the petitioner contends, all the processes applied by it to its mineral (or, as the respondent contends, only those which precede the sintering process) constitute ordinary treatment processes for the purpose of computing the petitioner's gross income from mining, and, thus, its percentage depletion deduction, for Federal income tax purposes, for the fiscal year involved.

RELEVANT STATUTE

The statutory provisions which govern this case are contained in Sections 611 and 613 of the Internal Revenue Code of 1954, 26 U.S.C. §§ 611 and 613 (Vol. 5, pp. 4396 and 4397), the full text of which is set out in Appendix C hereto, and the relevant provisions of which are as follows:

"§ 611. Allowance of deduction for depletion

"(a) General Rule.—In the case of mines, oil and gas wells, other natural deposits, and timber, there shall be allowed as a deduction in computing taxable income a reasonable allowance for

depletion and for depreciation of improvements, according to the peculiar conditions in each case; * * * "

"§ 613. Percentage depletion

"(a) General Rule. — In the case of the mines, wells, and other natural deposits listed in subsection (b), the allowance for depletion * * * shall be the percentage, specified in subsection (b), of the gross income from the property * * * .

"(b) Percentage Depletion Rates. — The mines, wells, and other natural deposits, and the percentages, referred to in subsection (a) are as follows:

* * * * * * *

"(3) 15 per cent—ball clay, bentonite, china clay, sagger clay, metal mines (if paragraph (2) (B) does not appiy), rock asphalt and vermiculite.

* * * * * * *

"(6) 15 per cent — all other minerals (including, but not limited to, * * * slate, * * *), except that, unless sold on bid in direct competition with a bona fide bid to sell a mineral listed in paragraph (3), the percentage shall be 5 per cent for any such other mineral when used, or sold for use, by the mine owner or operator as * * * concrete aggregates, or for similar purposes.

* * * * * *

"(c) Definition of Gross Income From Property.—For purposes of this section—

"(1) Gross income from the property.—The term 'gross income from the property' means, * * * the gross income from mining.

"(2) Mining. — The term 'mining' includes not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products, and so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto as is not in excess of 50 miles unless the Secretary or his delegate finds that the physical and other requirements are such that the ore or mineral must be transported a greater distance to such plants or mills.

* * * * * *

"(4) Ordinary treatment processes.—The term 'ordinary treatment processes' includes the following:

(A) In the case of coal—* * *;

(B) in the case of sulphur * * *;

(C) in the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude

mineral product—sorting, concentrating, and sintering to bring to shipping grade and form, and loading for shipment;

(D) in the case of lead, zinc * * *;

and

(E) the pulverization of talc, the burning of magnesite, and the sintering and nodulizing of phosphate rock."

STATEMENT OF THE CASE

Petitioner brought suit in 1962 in the United States District Court for the Eastern District of Virginia, Norfolk Division, for refund of Federal income taxes and interest thereon, in the aggregate amount of $31,979.70, which had been collected by the respondent from the petitioner for the petitioner's fiscal year ended March 31, 1958, invoking the jurisdiction of said Court under 28 U.S.C. §§1340, 1346(a)(1) and 1402.

The following facts were agreed upon by the parties in the Stipulation of Facts (the "stipulation") filed in the District Court (and in which the petitioner is referred to as the taxpayer and the respondent is referred to as the Government):

1. The taxpayer, at all times herein concerned, was (and still is) a corporation organized and existing under the laws of the State of Virginia, with its principal office in the City of Norfolk, Virginia, and kept its books and computed its tax liabilities on the basis of a fiscal year beginning April 1st and ending March 31st.

2. This action arises under the Internal Revenue laws of the United States of America and jurisdiction is

conferred by Title 28, USCA, Sections 1340, 1346(a)(1) and 1402.

3. This is an action for the recovery of Federal income taxes and interest assessed against and collected from the taxpayer by the Government for the taxable year ended March 31, 1958.

4. The taxpayer was during said taxable year and still is engaged in the business of extracting from the ground a weathered material and of applying thereto the following processes.

(a) The overburden, consisting of top soil, on the surface of the ground, is first removed.

(b) The weathered material lying below the top soil is then drilled and blasted and loaded on trucks, which carry said material to the taxpayer's plant located a short distance (approximately one-half mile) from the quarry.

(c) The material is dumped from the trucks into the primary crusher and screener, where it is crushed and screened and then conveyed by a conveyor belt to a stockpile, from which it is conveyed by a conveyor belt and bucket elevator to a rotary kiln.

(d) The material is fed into the high end of the rotary kiln (which is on an inclined axis) and as the kiln turns the material passes slowly from the higher end to the lower end of the kiln, from which heat is blown into the kiln.

(e) The material drops from the lower end of the kiln to the ground, where it stays long enough to become cool.

(f) The material is then placed, through the use of a clam shell bucket and crane, in the secondary crusher and screener, where it is crushed and screened and then loaded by a conveyor belt into freight cars.

5. No other material of any kind is added during the aforesaid treatment processes.

6. The trade name given by the taxpayer to the aggregate which it produces, through the aforesaid processes, is "Solite", and the taxpayer sells all the weathered material which it mines, after applying the above processes, to others who use it in the manufacture of building blocks and other building units.

7. The taxpayer does not use any of the Solite produced by it to manufacture any other product.

8. Under Section 613 of the Internal Revenue Code of 1954, as amended, the taxpayer was entitled to deduct, as a percentage depletion allowance, in computing its Federal income tax liability for the taxable year ended March 31, 1958, an amount equal to 5% of its gross income derived during said year from its mining, as therein defined.

9. A refund claim in proper form was duly and seasonably filed by the taxpayer with the District Director of Internal Revenue at Richmond, Virginia, on May 1, 1962, and said claim was rejected on September 17, 1962.

The petitioner believes that the evidence clearly establishes the additional facts hereinafter set out.

The petitioner's mineral, referred to in the stipulation as a "weathered material", is weathered slate which is extracted from a deposit in Buckingham County, Virginia, in what is commonly known as the Arvonia slate belt. In addition to the petitioner's deposit there are numerous other substantial deposits of such weathered slate which are not owned or controlled by the petitioner. There is no market whatsoever for weathered slate in its natural or raw state. The material has been thoroughly tested—with negative results—to determine its suitability or marketability for any purpose. The owners of other deposits of weathered slate, who must remove it in order to mine the underlying hard slate (used for roofing and other purposes), discard the weathered slate as unusable and unmarketable.

In conducting its business, the petitioner normally applies all the processes set out in subparagraphs (a) through (f) of paragraph 4, above, and all such processes are necessary in order to obtain a commercially marketable mineral product, namely, a lightweight aggregate. Said processes are those which are normally applied by miners of weathered slate in order to obtain therefrom a commercially marketable mineral product.

The heating process (set out in subparagraph 4(d), above) is a sintering process which causes an agglomeration of the raw mineral by incipient fusion. The process is applied, and is essential, to bring the mineral (through causing it to expand or bloat) to shipping grade and form and to make it commercially marketable. Petitioner's product, sold under the trade name of "Solite", is a crude mineral product which is used as a lightweight aggregate in making building units, such as blocks. Prior to the application of all the processes set out in paragraph

4 of the stipulation, the weathered slate is not of shipping grade and form and there is no market therefor.

The District Court denied recovery by petitioner in accordance with its opinion hereto attached as Appendix A.

Petitioner appealed to the United States Court of Appeals for the Fourth Circuit and said Court of Appeals affirmed in accordance with its opinion hereto attached as Appendix B.

The only issue in the case was whether the heating process, found by the District Court to constitute sintering, was an "ordinary treatment process" within the meaning of the general rule set out in subsection 613(c)-(2) or the specific rule set out in subsection 613(c)(4) of the applicable statute.

The District Court held that the "cut-off point" was not (using the language of the statute) "where the mineral became commercially marketable" but rather "under the teachings of *Cannelton, Longhorn Portland Cement,* and *Light Aggregates,* we find that the true test of the cut-off is *where the mineral first became suitable for industrial use or consumption,* and this is to be treated as though the miner sold the material to himself for processing."

The District Court also held that the petitioner's mineral was not sold as a crude mineral product and that the sintering was not for the purpose of bringing the weathered slate "to shipping grade and form, and loading for shipment," saying only that, "clearly the evidence shows that the lightweight aggregate is no longer custom-

arily sold as a 'crude mineral product' after it emerges from the rotary kiln" and, notwithstanding the fact that the chemical analyses of the raw material and the sintered material were substantially identical, "the X ray diffraction demonstrates a marked or radical chemical change or, as sometimes described, a compound change." No other basis was given for these holdings and the Court of Appeals stated only that they were adequately supported by the record and were not clearly erroneous.

The Court of Appeals further stated, citing the opinion of this Court in *United States* v. *Cannelton Sewer Pipe Co.*, 364 U.S. 76 (1960), "that percentage depletion cannot be used to give an advantage to the integrated miner-manufacturer which is not shared by nonintegrated miners and manufacturers," and then, after recognizing that the petitioner's weathered slate not only does not enjoy an actual market and that "unless used for processing in the final production of lightweight aggregate, it is universally discarded," relied on the *Cannelton* case and the decision of this Court in *Riddell* v. *Monolith Portland Cement Co.*, 371 U.S. 537 (1963), in holding that it is not even necessary that a market be available in order for the petitioner's mineral to be "commercially marketable" within the meaning of the statute. The Court of Appeals also appears to have considered the petitioner's mineral together with other minerals which are sometimes used for the production of lightweight aggregate—apparently disregarding the fact that such other minerals are suitable, and are salable and are sold, in their raw form for other uses—and stated that, "If there are miners of materials used in the production of lightweight aggregates who sell that material before employing the kiln process, then surely miners who them-

selves employ the kiln process are miner-manufacturers within the meaning of the *Cannelton* case," and concluded that the construction of the percentage depletion allowance statute contended for by the petitioner would give it "a decided competitive advantage over its nonintegrated manufacturer competitor" which the Court of Appeals thought was prohibited by the *Cannelton* case.

Finally, the Court of Appeals stated that, "We do not interpret the cases as requiring that a market be actually available to the taxpayer in order for its mineral to be 'commercially marketable' within the meaning of the statute," and that since the petitioner's mineral is physically susceptible of being transported, even though not economically feasible over a considerable distance, and since "others in the same industry" purchase "similar" materials for use in making a "product substantially the same" as the petitioner's, its conclusion was that the petitioner's weathered slate is "suitable for industrial use or consumption."

REASONS FOR GRANTING THE WRIT

The decision of the Court below represents a marked and drastic departure from the governing statute and from the decisions of this Court construing the same.

There are involved here important questions of Federal law which have not been, but should be, settled by this Court, and which have been erroneously answered by the lower Courts based upon what we believe to be gross misinterpretations of statements of this Court, or, if the lower Courts have not misinterpreted the statements of this Court, then, at least in part, upon what we

believe are demonstrably erroneous statements of this Court.

Both the District Court and the Court of Appeals relied almost exclusively on supposed holdings of this Court in the *Cannelton* and *Monolith* cases and on the decision of the Court of Appeals for the Eighth Circuit in *United States* v. *Light Aggregates, Inc.*, 343 F. 2d 429 (1965). The statements of this Court which were relied on by the Court below (and by the Court of Appeals for the Eighth Circuit in the *Light Aggregates* case) were not necessary to the decisions in the *Cannelton* or *Monolith* cases, and we do not believe that such statements of this Court should be (and certainly were not intended to be) so torn out of their context or applied to a factual situation so different from those before this Court as to amount to complete disregard or emasculation of the controlling statute. Nevertheless, such is the existing situation.

The Court of Appeals has also interpreted the *Cannelton* case as requiring the disallowance of petitioner's sintering process because petitioner would otherwise have "a decided competitive advantage over its nonintegrated manufacturer competitor." The quoted words were taken out of context from the *Cannelton* opinion of this Court. But the *Cannelton* opinion was dealing with integrated and nonintegrated miners of the same marketable mineral, while the Court below is referring to two different minerals, one of which could be sold in the raw state and used for many purposes while the other was not marketable and not usable for any purpose except further processing. Clearly, the position taken by the Court below is an invalid extension of the guides set forth in the *Cannelton* case. Had Congress intended, by the use of percentage

depletion deductions, to put all producers of lightweight aggregates on the same competitive footing, it undoubtedly would not have granted a percentage depletion rate of fifteen per cent to vermiculite or ten per cent to perlite, both of which are natural lightweight aggregates in competition with petitioner's product.

We do not criticize the results in *Cannelton* or *Monolith* since the opinions clearly indicate that the particular minerals involved were commercially marketable at the point which this Court held was the "cut-off" point for the purpose of the percentage depletion deduction.

However, in the *Cannelton* opinion, after succinctly stating the legislative history and the controlling provisions of the statute, clearly demonstrating that percentage depletion deductions are to be based upon gross income from an extracted, salable mineral or mineral product without regard to the intrinsic value of the mineral in the original deposit, this Court said:

> "We note that the Congress even states the steps in each permissible process, and in addition specifically declares some processes not to be 'ordinary treatment' ones, *viz.*, 'electrolytic deposition, roasting, thermal or electric smelting, or refining.' Furthermore, none of the permissible processes destroy the physical or chemical identity of the minerals or permit them to be transformed into new products. From this legislative history, we conclude that Congress intended to grant miners a depletion allowance based on the constructive income from the raw mineral product, *if marketable in that form,* and not on the value of the finished articles." [Italics supplied]

Based upon the second sentence quoted above, and ignoring the balance, the respondent has argued, and the Courts below have held, that the petitioner's sintering process, because it results in a physical and chemical change, cannot be a permissible process—notwithstanding the evidence before both said Courts that several of the processes which are specifically enumerated in the statute as ordinary treatment processes do, by their very nature, cause physical and chemical changes and do destroy the physical and chemical identity of the minerals involved to an equal or greater degree than is the case with the sintering process applied by petitioner to its mineral. Thus, it is inconceivable that the Courts below have construed the statements of this Court as they were intended.

Also, in the *Cannelton* opinion, this Court said,

> "The findings are that three-fifths of the fire clay produced in Indiana in 1951 was sold in its raw state. This indicates a substantial market for the raw mineral. In addition, large sales of raw fire clay and shale were made across the river in Kentucky. This indicates that fire clay and shale were 'commercially marketable' in their raw state unless that phrase also implies marketability at a profit. We believe it does not. Proof of these sales is significant not because it reveals an ability to sell profitably—which the respondent could not do—but because the substantial tonnage being sold in a raw state provides conclusive proof that, when extracted from the mine, the fire clay and shale are in such a state that they are ready for industrial use or consumption—in short, they have passed the 'mining' state on which the depletion principles operate."

And in the *Monolith* case, this Court said with reference to the statutory term, "mining":

> "In *United States* v. *Cannelton Sewer Pipe Co.*, 364 U.S. 76 (1960), we considered at some length the application of this term to the mining industry and held that the statutory percentage depletion allowance on the gross income of an integrated mining operator should be cut off at the point where the mineral first became suitable for industrial use or consumption. After careful study of the record here we believe that this case is controlled by *Cannelton*. We concluded there 'that Congress intended to grant miners a depletion allowance based on the constructive income from the raw mineral product, if marketable in that form, and not on the value of the finished articles.' 364 U.S., at 86. We found that 'the cut-off point where "gross income from mining" stopped has been the same' ever since the first depletion statute, namely, 'where the ordinary miner shipped the product of his mine.' "

The respondent has argued, and the Courts below have held, that by the above quoted language this Court has thrown out the test of "commercial marketability" which is provided by the statute and has substituted an entirely new and different test, to-wit: "suitable for industrial use or consumption," which has nothing to do with salability or marketability. Again, it is inconceivable that such is in accord with the intention of this Court.

We believe that the Courts below have misconstrued the statements of this Court in the *Cannelton* and

Monolith cases and that they will continue to do so unless and until this Court provides guidance to return them to the proper course and makes it clear that the provisions of the statute are to control.

If, as the District Court said, the true test is not "where the mineral became commercially marketable" but, instead, "where the mineral first became suitable for industrial use or consumption," and if, as the Court of Appeals said, it is not even required that a market be available in order for a mineral to be "commercially marketable," we believe that this Court ought to say so in clear and explicit terms.

If, on the other hand, the true test is "where the mineral became commercially marketable," and "marketable" means "able to market," we likewise believe that this Court should say so in such clear terms as to leave no further doubt.

Since there can be no question but that the statutory provisions are controlling, it is necessary, for the proper administration of the taxing statute, that this Court consider the applicability of subsection 613(c)(4)(C) and the specific processes which are thereby stated to be included within the term "ordinary treatment processes."

Since the legislative history and the purpose of the percentage depletion statutes have heretofore been so extensively considered by this Court, any extended discussion thereof here seems unnecessary. However, a few brief observations in respect thereto may be helpful. Percentage depletion has no meaning or application outside of the income tax law. While for general accounting purposes it is proper to reserve and deduct from earnings

an amount which reflects the exhaustion of a mineral deposit, such reservation is based upon an entirely different concept, and the reserved amount is measured solely by the cost of the deposit. Percentage depletion, on the other hand, being strictly an income tax concept, has no relation whatever to general accounting or to the cost or value of minerals in place but is based on and measured solely by the income derived therefrom. The rate of percentage depletion for a particular mineral is set by the Congress, not with regard to the cost or value of a given deposit or of all deposits, but rather with the view of providing a tax incentive which "encourages extensive exploration and increasing discoveries of additional minerals to the benefit of the economy and strength of the Nation." *U.S.* v. *Cannelton Sewer Pipe Co.*, supra.

Having no foundation on general accounting principles but being a purely statutory concept for the purposes of income taxation only, we have no guide to the understanding of percentage depletion except the statutes which create it and the proper interpretation of those statutes by the courts. Almost from the beginning, the Congress and the Treasury Department have been at odds with respect to the wisdom of percentage depletion, particularly the alleged "loss" of revenues resulting from the higher allowances thereunder as compared with cost depletion. As was said by the Courts of Appeals for the First and Ninth Circuits in *Dragon Cement Company* v. *United States,* 244 F. 2d 513 (1957), cert. denied, 355 U.S. 833 (1957), and *Monolith Portland Cement Co.* v. *Riddell,* 301 F. 2d 488 (1962), respectively:

> "The allowance for depletion has been a controversial subject for years, and officials of the executive branch have sought from time to time,

> with conspicuous lack of success, to persuade the Congress to eliminate some of its alleged over-generous features. See Mertens, Law of Federal Income Taxation Section 24.04 (1954)."

But each time the Congress has acted, it has been more, rather than less, generous with respect to the deductions allowed and has continually broadened the statute to include more and more minerals. Turning to the courts, the Treasury for years argued for its own interpretation of the percentage depletion statutes and the courts consistently rejected the apparent attempts to avoid or narrow the Congressional intent and purpose, saying, "We are not concerned with the validity of this theory or with the statutory policy. Our sole function is application of the Congressional mandate." *U.S.* v. *Cannelton Sewer Pipe Co.*, supra, or "We are not concerned with the wisdom or policy of the statutory allowance as Congress wrote it and meant it." *Dragon Cement Company* v. *U. S.*, supra; *Monolith Portland Cement Co.* v. *Riddell*, 301 F. 2d 488.

Prior to the decision in *Cannelton*, a long line of cases in the District Courts and the Courts of Appeals had uniformly held that the taxpayers therein were entitled to treat as ordinary treatment processes, for the purpose of determining their gross income from mining (and, accordingly, their percentage depletion deductions), all the treatment processes normally applied by the respective taxpayers in order to obtain the first mineral product which could be commercially marketed. In construing the statutory term "commercially marketable mineral product or products" these cases uniformly held that the mineral product was not commercially marketable unless and until an actual, sufficient market existed

therefor (evidence of sales of very small amounts of a particular mineral or of an inconsequential portion of the mineral produced was held to be not sufficient to establish the existence of a commercial market). Two of these cases, hereinafter referred to, held that "commercially marketable" also required marketability at a profit. Among these earlier cases were *Cherokee Brick and Tile Co.* v. *United States,* 218 F. 2d 424 (CA-5, 1955); *The Hitchcock Corp.* v. *Townsend,* 232 F. 2d 444 (CA-4, 1956); *Sapulpa Brick and Tile Corp.* v. *United States,* 239 F. 2d 694 (CA-10, 1957); *Merry Brothers Brick and Tile Co.* v. *United States,* 242 F. 2d 708 (CA-5, 1957), cert. denied, 355 U.S. 824 (1957); and *Dragon Cement Co.* v. *United States,* supra.

The Treasury Department continued to litigate in its attempts to restrict percentage depletion allowances, and continued to present not only such arguments as were later to be held valid but additional arguments which would ignore the clear terms of the statute. And the invalid arguments continued to be rejected.

In 1960, this Court decided the case of *United States* v. *Cannelton Sewer Pipe Company,* 364 U.S. 76, and in 1963, the case of *Riddell* v. *Monolith Portland Cement Co.,* 371 U.S. 357. These two cases were actually narrow in scope and application and fell far short of adopting the strained interpretation of the statute for which the respondent contends. Nevertheless, they seem to have given added impetus to the respondent's attacks and have been the subject of study and interpretation by the Tax Court, the Court of Claims, several District Courts and several Courts of Appeals in subsequent cases. And in each subsequent case the Government has sought not only its own interpretation of the statutory provisions (which we be-

lieve this Court refused to adopt in either *Cannelton* or *Monolith*) but has attempted to persuade (and in this case has been notably successful in persuading) the courts to extend the application of the *Cannelton* and *Monolith* cases far beyond the limits of their holdings. There had, of course, been no material change in the applicable statute.

In the *Cannelton* case the taxpayer involved, during its taxable year ended on November 30, 1951, owned and operated an underground mine from which it produced fire clay and shale in the proportions of 60 per cent and 40 per cent, respectively. The clay and shale were transported by truck about one and one-half miles from the taxpayer's mine to its plant at Cannelton, Indiana, where it was processed and fabricated into vitrified sewer pipe, flue lining and related products. The processes applied to the clay and shale included grinding into a pulverized form, mixing with water in a pug mill until it became a plastic mass, forming by machines into the shape of the finished ware desired, application of heat to remove all water, vitrification by application of heat in kilns, cooling, grading, and shipping or storing. Since the Cannelton operation required clay and shale having plasticity, special drying qualities and the ability to withstand high temperatures, not all clays and shales were suitable for Cannelton's operations. The Cannelton clay and shale, however, could be used for the same purposes as other fire clays and shales mined in the same general area.

The *Cannelton* record showed, and the District Court found, that in 1951 there were substantial sales of raw fire clay and shale in Indiana, mostly in the vicinity of Brazil about 140 miles from Cannelton, at an average price of $1.60 to $1.90 per ton for clay and $1.00 per ton

for shale, and in Kentucky, across the river from the taxpayer's plant, fire clay and shale of the same grade were mined and sold before, during and subsequent to 1951.

After briefly reviewing the legislative history and the provisions of the controlling statute (Sec. 114(b)(4)(B) of the Internal Revenue Code of 1939) this Court stated:

> "* * * From this legislative history, we conclude that Congress intended to grant miners a depletion allowance based on the constructive income from the raw mineral product, *if marketable in that form,* and not on the value of the finished articles. [Italics supplied]
>
> "III. The findings are that three-fifths of the fire clay produced in Indiana in 1951 was sold in its raw state. *This indicates a substantial market for the raw material.* In addition, large sales of raw fire clay and shale were made across the river in Kentucky. This indicates that fire clay and shale were 'commercially marketable' in their raw state *unless that phrase also implies marketability at a profit.* We believe it does not. Proof of these sales is significant not because it reveals an ability to sell profitably—which the respondent could not do—but because the substantial tonnage being sold in a raw state provides conclusive proof that, when extracted from the mine, the fire clay and shale are in such a state that they are ready for industrial use or consumption—in short, they have passed the 'mining' state on which the depletion principles operate. * * * [Italics supplied]

* * * * * *

"In view of the finding that substantial quantities—in fact, the majority—of the tonnage production of fire clay and shale were sold in their raw state, we believe that respondent's mining activity during the year in question would come under clause (iii) of the section here involved.[1] That clause includes 'minerals which are customarily sold in the form of a crude mineral product.' We believe that the Congress intended integrated mining-manufacturing operations to be treated as if the operator were selling the mineral mined to himself for fabrication. It would, of course, be permissible for such an operator to calculate his 'gross income from mining' at the point where 'ordinary' miners—not integrated—disposed of their product. All processes used by the nonintegrated miner before shipping the raw fire clay and shale would under such a formula be available to the integrated miner-manufacturer to the same extent but no more." [Footnote added]

As can be seen from the foregoing, this Court did not determine that the depletion allowance should be based on the constructive income from the raw mineral product unless *the product were marketable in that form.* Thus, the cut-off point is that point where a commercial market exists or would exist if the miner wished to sell his mineral. It is not necessary that the miner be able to sell *profitably* in such market or that he actually sell therein, but the term "commercially marketable" does mean that the mineral or mineral product must be com-

1. This clause is identical to Section 613(c)(4)(C) of the Internal Revenue Code of 1954 as the same was in effect during Solite Corporation's taxable year ended March 31, 1958.

mercially marketable in the sense that someone will buy the mineral or mineral product if it were offered for sale.

In referring to an "integrated miner-manufacturer" we believe this Court clearly meant only the miner who by-passed the available market, as the Cannelton Sewer Pipe Company did, in order to realize greater profits by the application of additional processes. (If, rather than selling its lightweight aggregate in the existing market therefor, the petitioner herein applied further processes or used its product in the manufacture of building blocks or other finished units, it would then be an integrated miner-manufacturer, as was the Cannelton Sewer Pipe Company, and would not be permitted to compute its percentage depletion allowance upon the processes applied after it obtained the commercially marketable mineral product, lightweight aggregate. But the petitioner does not do so—it is not an integrated miner-manufacturer—it sells its entire production of the crude mineral product at the first available opportunity.)

It should be noted that with respect to the prior cases on which the Cannelton Sewer Pipe Company relied, this Court cited *United States* v. *Cherokee Brick and Tile Co.*, supra, and *United States* v. *Merry Brothers Brick and Tile Co.*, supra, but pointed out that these cases went off on factual concessions not present in the *Cannelton* case. This Court also stated that those two cases "have been pyramided into a statistically imposing number of cases, predicated upon one another" and that "close analysis indicates that they either go off on concessions or findings not present here, or deal with controversies over particular treatment processes claimed as 'ordinary' in the industry involved." This Court did not, either expressly or impliedly, say that those cases were erroneously

decided, but that "it is sufficient to say that on their facts they are all distinguishable." A review of the opinions by the District Courts and the Court of Appeals in the *Merry Brothers* and *Cherokee* cases reveals that the only factual concessions therein which could have been the distinguishing features of those cases were that only negligible amounts of the brick and tile clay there involved were actually sold before it was put into the form of brick and tile and that the processes applied by the taxpayers in those cases were those ordinarily applied by miners of brick and tile clay. It is true, of course, that the *Merry Brothers* and *Cherokee* cases involved brick and tile clay while the *Cannelton* case involved fire clay and shale, minerals which are separately classified under the depletion statute, but this difference could not be the subject of the "factual concessions" and such a difference was more likely the basis of the Court's statement (which could have application here) that some of the prior cases "deal with controversies over particular treatment processes claimed as 'ordinary' in the industry involved."

In the *Cannelton* case, this Court expressly repudiated the profitability test which had been adopted in *Commissioner* v. *Iowa Limestone Co.*, 269 F. 2d 398 (1959), and *Bookwalter* v. *Centropolis Crusher Co.*, 272 F. 2d 391 (1959), and having found an existing commercial market for the Cannelton Company's raw clay and shale, the Court held that it was immaterial that the company did not desire to sell in that market or that (as the taxpayer there contended) such clay and shale could not be marketed by the taxpayer at a profit.

In *Riddell* v. *Monolith Portland Cement Co.*, 371 U.S. 537, this Court quoting from its *Cannelton* opinion said "that Congress intended to grant miners a depletion

allowance based on the constructive income from the raw mineral product, *if marketable in that form,* and not on the value of the finished articles" [italics supplied], and that "the cut-off point where 'gross income from mining' stopped" is "where the ordinary miner shipped the product of his mine." Then, based upon the record before it which showed that *there were substantial sales of crushed limestone in an actual existing commercial market therefor in California* (where Monolith carried on its business), this Court concluded that, "It therefore appears from this record that the 'product' with which the Act deals here is the taxpayer's product at the point when 'mining' terminated, i.e., when it reached the crushed limestone stage," and stated in its footnote that:

> "In this connection crushed limestone was not only 'marketable in that form' but, according to the Preprint from Bureau of Mines Minerals Yearbook, 1952, Stone, p. 26, an exhibit in the record, it was actually sold in California in 1952 in an amount exceeding 1,500,000 tons. Sales in the United States for that year exceeded 216,000,000 tons. Both of these figures exclude the tonnage used in the manufacture of cement. A stipulation in the record shows that limestone sold or used for all purposes totalled almost 300,000,000 tons in 1952.".

Again, in the *Monolith* case this Court held that the cut-off point for the allowable processes is where the evidence shows substantial sales (more than 1,500,000 tons in California and more than two-thirds of the limestone produced in the United States was sold in the crushed limestone form) in an existing commercial market for the particular mineral. It is important to

note that this Court did not, either in the *Cannelton* case or the *Monolith* case, attempt to distinguish, as the respondent would have it do, between processes which are "essentially mining" and those which are "essentially manufacturing" but rather based its decisions upon evidence in the records that at the respective cut-off points substantial amounts of the minerals involved were actually sold, thereby establishing the fact that the minerals were "marketable in that form."

The Court of Appeals for the Tenth Circuit, in rendering its opinion in *Portland Cement Company of Utah* v. *United States,* 315 F. 2d 169 (1963), had before it the decisions of this Court in the *Cannelton* and *Monolith* cases. In a very brief opinion the Court stated that, in point of material facts, the *Monolith* case and the case before it closely paralleled each other. And since this Court in *Monolith* had found that crushed limestone was sold in substantial quantities, thus demonstrating that it was commercially marketable in that form, and that the property of Monolith "with which the statute allowing depletion dealt was the mineral product when it reached the crushed limestone state," the basis of depletion of the taxpayer before it was "limited in like manner to the constructive income from the limestone when it reached the crushed stage." This decision is clearly based on the finding of this Court in the *Monolith* case that an actual commercial market existed for crushed limestone, thus showing that the taxpayer could, if it desired, commercially market its product when it reached the crushed limestone stage.

The decision by the Court of Appeals for the Fourth Circuit in *Virginia Greenstone Company, Incorporated* v. *United States,* 308 F. 2d 669 (1962), also warrants dis-

cussion. In that case it was held that the cut-off point did not require actual sales of the taxpayer's greenstone quarry block where (1) the taxpayer owned and controlled the only source of the mineral involved, (2) the taxpayer could, if it desired, sell its greenstone quarry block to others for finishing in plants being operated for finishing of other similar dimension stone, and (3) the absence of an actvie market was solely the result of the taxpayer's refusal to sell. The taxpayer, in Lynchburg, Virginia, mined, cut and finished greenstone for use as ornamental or dimension stone on and in buildings. The greenstone was removed from the quarry in large blocks which were transported by truck to the finishing plant located approximately one and one-quarter miles from the quarry, where they were cut, with gang-saws, into slabs of the desired thickness which varied according to customers' specifications between seven-eighths of an inch and one and one-quarter inches. The slabs were then cut to specified lengths and widths after which their surfaces were smoothed and finished by sand-rubbing to produce a product known as sand-finished greenstone. Some customers' orders required further polishing, honing, buffing, notching or drilling of, or carving of letters and numerals into, the outside surface of the slabs and substantial orders were received for sand-finished greenstone without further polishing, notching, drilling or carving. The taxpayer contended that its sand-finished greenstone was its first marketable product. The taxpayer was the only producer of greenstone in the United States and sought to promote the use of greenstone rather than other dimension stone such as marble or granite with which it competed, the color being the principal selling point.

The taxpayer there argued that its first marketable product was not quarry block, as the government contended, because it had not sold any of its quarry block prior to processing the greenstone into sand-finished greenstone. The Court of Appeals said:

> "There is no other producer of greenstone in the United States. Since the taxpayer is the sole producer of such stone and actively promotes its use, it is not surprising that it is the recipient of the greenstone orders, and that in the years in question it sold no quarry block to others. On infrequent occasions, it received inquiries about the sale of quarry block for processing in other dressing plants, but these were insignificant in the quantity of material involved. Plainly there was no active market for greenstone quarry blocks.
>
> "It does not follow, however, that the taxpayer could not have marketed its quarry block had it sought to do so. * * *
>
> "For all that appears, therefore, the absence of an active market for greenstone quarry block is attributable to the taxpayer's volition. It controlled the only source of supply, * * *."

With reference to the history of percentage depletion and the *Cannelton* case the Court of Appeals said:

> "Percentage depletion for the extractive industries has a long history, so often reviewed it need not be recounted here. It discloses a liberal congressional approach to the allowance of the deduction and to the inclusion of related processes within the compass of the favored mining operations. This fact led to decisions that integrated

> miner-manufacturers were entitled to percentage depletion on the basis of the gross income from the sale of the first marketable product of the manufacturing processing if there was no active market in which the product of the mine could be *profitably* sold without conversion into manufactured products. [Italics supplied]
>
> "That approach was halted by the decision of the Supreme Court in *United States* v. *Cannelton Sewer Pipe Co.* * * *"

We think that the Court of Appeals in the *Virginia Greenstone* case correctly viewed the *Cannelton* case only as rejecting the profitability test in determining whether a given mineral was commercially marketable.

Light Aggregates, Inc. v. *United States,* supra, is a more recent case, decided by the Court of Appeals for the Eighth Circuit. In that case the taxpayer produced a lightweight aggregate from clay and shale (terms which, the District Court stated in its opinion reported at 225 F. Supp. 253, substantially have reference to the same material) which it extracted from its mine located about twelve miles from its plant. The opinion shows that while there were no actual sales of the raw clay by the taxpayer involved, the evidence indicated that of the "miscellaneous clays" mined (which classification included that taxpayer's mineral) from 1952 to 1961 an average of about 1,315,000 tons was sold annually by producers in its raw state.

At this point it becomes important to consider the phrase "fit for industrial use or consumption" which has been used in connection with percentage depletion. Orig-

inally coined, we believe, by the Treasury Department to narrow the statutory phrase "commercially marketable" and to apply a new test of its own for the proper cut-off point for percentage depletion in lieu of the unsatisfactory (from the Treasury's view) test supplied by Congress, this phrase appears to have been first used by the courts in the *Cannelton* opinion. In that case, this Court stated:

> "The findings are that three-fifths of the fire clay produced in Indiana in 1951 was sold in its raw state. *This indicates a substantial market for the raw mineral.* In addition, large sales of raw fire clay and shale were made across the river in Kentucky. *This indicates that fire clay and shale were 'commercially marketable' in their raw state unless that phrase also implies marketability at a profit.* We believe it does not. Proof of these sales is significant not because it reveals an ability to sell *profitably*—which the respondent could not do—but because the substantial tonnage being sold in a raw state provides conclusive proof that, when extracted from the mine, the fire clay and shale are in such a state that they are ready for industrial use or consumption—in short, they have passed the 'mining' state on which the depletion principles operate. * * *" [Italics supplied]

Seizing upon the last portion of the last sentence quoted above, and ignoring all the rest, the respondent has argued that this Court intended to disregard the statutory language and proclaim a new test of its own which has nothing to do with marketability. The Government attempts to reverse the Court's words and argue that a finding of "fit for industrial use or consumption"

provides conclusive proof of "commercial marketability." Clearly, such an argument is erroneous. This Court obviously never intended to disregard the statute and embark on a course of judicial legislation of its own. The only true meaning which we believe can be ascribed to these words of the Court is that which is clearly stated, i.e., the proof of commercial marketing of a given mineral by others constitutes proof of the commercial marketability of that same mineral by the miner concerned.

In the *Monolith* case, this Court said:

> "The Congress further provided * * * that included within the term 'mining' were 'the ordinary treatment processes normally applied by mine owners or operators in order to obtain the *commercially marketable mineral product* * * *.' [Italics supplied]
>
> "In *United States* v. *Cannelton Sewer Pipe Co.*, 364 U.S. 76 (1960), we considered at some length the application of this term to the mining industry and held that the statutory percentage depletion allowance on the gross income of an integrated mining operator should be cut off at the point where the mineral first became suitable for industrial use or consumption. After careful study of the record here we believe that this case is controlled by *Cannelton*. We concluded *there* [italics supplied] 'that Congress intended to grant miners a depletion allowance based on the constructive income from the raw mineral product, *if marketable in that form,* [italics supplied] and not on the value of the finished articles.' 364 U.S., at 86. We found that 'the cut-off point where

> "gross income from mining" stopped has been the same' ever since the first depletion statute, namely, 'where the ordinary miner *shipped* [italics supplied] the product of his mine." *Id.,* at 87. It therefore appears from this record that the 'product' with which the Act deals here is the taxpayer's product at the point when 'mining' terminated, i.e., when it reached the crushed limestone stage."[1]

Notwithstanding the language used in that opinion, however, the respondent again tries to ignore portions thereof and argue that this Court has disregarded the test established by the Congress and has substituted a new one of its own. This Court clearly did no such thing.

Under the *Cannelton* and *Monolith* cases there can be no finding that a mineral is "fit for industrial use or consumption" (if that is to be the cut-off point for percentage depletion) until the mineral has reached the form in which it is commercially marketable and the miner can ship the product of his mine.

We submit that the Court of Appeals for the Eighth Circuit misconstrued the *Cannelton* and *Monolith* cases when in its opinion in the *Light Aggregates* case, it said that they establish the principles that (1) Congress intended to grant miners a depletion allowance based only on the constructive income from the *raw* material produced, and (2) the percentage depletion allowance should be cut off at a point where the mineral first be-

---

1. At this point in its opinion the Court appended a footnote pointing out that crushed limestone was not only "marketable in that form" but was actually sold in tremendous quantities.

came suitable for industrial use or consumption—unless these statements of the Court of Appeals are construed to mean (a) that "raw" materials continue to be raw materials until after the application of all the processes provided for in the statute (i.e., they could not cease to be "raw" merely because of the application of permissible nonextractive processes such as the sintering of certain minerals, the burning of magnesite or the sintering and nodulizing of phosphate rock), and (b) that a mineral or mineral product must first be shown to be commercially marketable before it can be deemed suitable for industrial use or consumption.

Perhaps the Court was correct as to the proper cut-off point in the *Light Aggregates* case since the evidence there showed that a substantial market actually existed for clays of the type there under consideration and substantial amounts were actually sold in the raw, unprocessed form, but the opinion in that case shows clearly that the *Cannelton* and *Monolith* opinions are being misinterpreted.

But the ultimate error is illustrated in the opinion of the District Court in this case, wherein it is said:

> "It is, of course, argued that the cut-off point should be where the mineral became commercially marketable but, under the teachings of *Cannelton, Longhorn Portland Cement,* and *Light Aggregates,* we find that the true test of the cut-off is *where the mineral first became suitable for industrial use or consumption,* and this is to be treated as though the miner sold the material to himself for processing."

And also in the opinion of the Court of Appeals below, wherein it is said:

> "We do not interpret the cases as requiring that a market be actually available to the taxpayer in order for its mineral to be 'commercially marketable' within the meaning of the statute."

Clearly, such an application here of a test to determine "where the mineral first became suitable for industrial use or consumption" rejects the controlling language of the statute and substitutes the Treasury Department test in a way never done or intended to be done by this Court.

The evidence in the case at bar is clear and undisputed that there is no market wherein weathered slate can be sold, either profitably or unprofitably, prior to the application of all the petitioner's processes. The testimony also conclusively shows that there are substantial other deposits of this identical slate, that the taxpayer does not own or control the supply of weathered slate, that the owners and operators who remove weathered slate from such other deposits know of no other use therefor or of any market therefor and discard their weathered slate as useless refuse. Clearly, if any market existed for weathered slate prior to the application of the processes which the taxpayer applies, then the owners of the other weathered slate deposits would sell their mineral rather than discard it.

The statutory language clearly shows, and the courts have repeatedly held, that the word "mining" (as used in the statute) embraces all the treatment processes normally applied in order to obtain the commercially mar-

ketable mineral product. Accordingly, under the facts of a particular case, the includable processes may well go far beyond the *ordinary concept* of mining operations. Some of the processes specifically defined and allowed as ordinary treatment processes in Section 613(c)(4) are clearly not a component part of "mining" as that term is ordinarily used. The Senate Finance Committee Report on Section 613(c)(4) explains the purpose of the listing of certain processes in that section:

> "* * * The purpose of the provision is to make certain that the ordinary treatment processes which a mine operator would normally apply to obtain a marketable product should be considered as a part of the mining operation, and to give reasonable specification of what are to be considered such processes for various kinds or classes of mines." Senate Report No. 627, 78th Congress, First Session, 23, 1944 C.B. 991.

And no court has ever held that Section 613(c)(4) is an exclusive listing of the included processes. This section was not intended to limit the provisions of Section 613(c)(2) but was intended to amplify them to provide for certain specific ordinary treatment processes as an illustration of how that section should be interpreted and applied.

Section 7701(b) of the Internal Revenue Code of 1954 (the Internal Revenue Title) provides:

> "(b) INCLUDES AND INCLUDING —The terms 'includes' and 'including' when used in a definition contained in this title shall not be deemed to exclude other things otherwise within the meaning of the term defined."

The uncontradicted evidence in this case clearly shows that all of petitioner's processes are included within the definition of mining as set out in Section 613(c)(2).

The respondent introduced certain depositions in evidence by which it apparently hoped to show that a lightweight aggregate can be made, by processes similar to those of the petitioner, from clays, shales, stones and slates other than the type of weathered slate used by the petitioner and that such clays, shales and other materials can be sold for other uses (such as the making of brick or for road construction purposes) without applying a kiln or sintering process. Obviously, these depositions were intended to support an argument that, and the Court of Appeals seems to have adopted the view that, if such other minerals can be sold for such other uses without applying a sintering process, then the petitioner's weathered slate should be placed in the same category with such other minerals (even though petitioner's weathered slate is not usable for any such other purposes) and treated as being commercially marketable after the primary crushing thereof. But the question here is not whether any such other mineral is commercially marketable but whether weathered slate is commercially marketable prior to the application of the heating process. To use the language of this Court in *Cannelton,* this case "deal[s] with controversies over particular treatment processes claimed as 'ordinary' in the industry involved," i.e., with the mining and processing of weathered slate.

The said depositions deal with minerals which are entirely different from weathered slate, and some of them also deal with businesses that were not even in operation

during the time with which we are here concerned (the petitioner's taxable year ended March 31, 1958).

The respondent knows that weathered slate (the material which the petitioner mines and uses) is not marketable prior to the application of the sintering process, and did not attempt to introduce any evidence whatsoever tending to show the existence of a market therefor. Moreover, the evidence shows clearly that the absence of any market is not the result of any power which this petitioner possesses. The respondent therefore relies on its old argument (which has been consistently rejected by most of the courts) that any process which causes a chemical or mineralogical change is not an "ordinary treatment process."

There is no question but that certain chemical and mineralogical changes occur during the application of the taxpayer's processes to its weathered slate. This has never been a source of contention. Even the crushing causes both a physical change and a chemical change (from the exposure of the material to air and moisture).

The question of the effect of the changes which take place during a treatment process has been considered several times in cases such as *Merry Brothers Brick and Tile Co.* v. *United States,* supra, and *Dragon Cement Co.* v. *United States,* supra. The respondent's argument on this point can probably be given no better answer than that given by the Court of Appeals for the Fifth Circuit in the *Merry Brothers* case and the Court of Appeals for the First Circuit in the *Dragon Cement* case. Were it not for the statements made in the opinion in *Light Aggregates, Inc.,* supra, it would appear that the argument is so manifestly specious that it would not merit any

further discussion. But, it is submitted, the reasoning of the Court in that case, as to the proper interpretation of *Cannelton,* is erroneous since it is based upon erroneous premises: First, that none of the processes permitted by the statute destroy the physical or chemical identity of the minerals; second, that the term "suitable for industrial use or consumption" is equivalent to the end of those processes which, apart from the percentage depletion statutes, are normally considered as mining, i.e., the purely extractive processes; and, third, that *Cannelton* teaches that all "manufacturing" processes are excluded from "mining".

In dealing with such first erroneous premise (which is, of course, based upon a statement of this Court in *Cannelton*) it should be noted, first, that Section 613 of the Internal Revenue Code of 1954, which governs this case, specifically provides, in subsection (c) (4) thereof, that the term "ordinary treatment processes" includes, in the case of iron ore, bauxite, ball and sagger clay, rock asphalt and minerals which are customarily sold in the form of a crude mineral product, the sintering thereof to bring to shipping grade and form, and also includes (under subsection 613(c) (4) (E)) the burning of magnesite and the sintering and nodulizing of phosphate rock; second, that the uncontradicted and incontrovertible evidence in this case shows that any sintering process necessarily involves physical, chemical and mineralogical changes; third, the undisputed expert testimony in this case clearly shows that in the sintering of certain iron ores the mineralogical and chemical changes would be as great as or greater than those occurring in the sintering of the petitioner's weathered slate; fourth, that the physical, mineralogical and chemical changes

in the burning of magnesite and the sintering of phosphate rock would be greater than occurs in the taxpayer's weathered slate; fifth, that in the sintering of iron ore glass is formed, some of the original minerals disappear and other synthetic minerals are formed; sixth, that in the sintering of iron ores, in the burning of magnesite and in the sintering of phosphate rock the original physical, mineralogical and chemical identities of the minerals are destroyed; seventh, that in the sintering of magnetite (an iron ore) in order to bring the said ore to shipping grade and form, the original magnetite oxidizes (a chemical reaction) and a considerable portion of the magnetite is converted to hematite; eighth, that in the sintering of limonite (iron) ores the original mineral is converted to the anhydrous ferric oxide or hematite form and the resulting mineral is entirely different from the original mineral; ninth, that in the sintering of siderite (iron) ores "a whole gamut of minerals" occur which do not occur in the original mineral at all; and tenth, in the burning of magnesite a complete mineralogical change occurs, the magnesite changes to periclase, a magnesium oxide, and the chemical identity of the magnesite is destroyed.

Thus, the statement that none of the permissible processes destroy the physical or chemical identity of the minerals, if that is taken to mean that substantial physical or chemical changes do not therein occur or that the statute precludes a process such as petitioner's sintering, is simply erroneous, and *Cannelton* cannot be correctly urged in this case as the basis for the cut-off point being at that stage of processing where the mineral undergoes chemical or physical changes.

Such second premise has been previously discussed

herein. The third is clearly erroneous in that it would exclude any process which, in the ordinary sense and apart from the depletion statute, would be considered as "manufacturing" even though such process is an ordinary one normally applied by mine owners or operators in order to obtain a commercially marketable mineral or mineral product and thus clearly within "mining" for this purpose.

We believe that the evidence clearly shows that all of the taxpayer's treatment processes (including the heating process) are the ordinary treatment processes normally applied by miners of weathered slate in order to obtain a commercially marketable mineral product, and that prior to the application of all such processes there is no market of any kind in which weathered slate can be sold. It is unnecessary to go beyond Section 613(c)(2) to support the petitioner's right of recovery; however, if we stop there, the confusion which has arisen in the administration of the taxing statutes will not have been eliminated but will continue and perhaps increase. Therefore, we believe that this Court must consider the provisions of Section 613(c)(4)(C) which specifically provide, with respect to "minerals which are customarily sold in the form of a crude mineral product" (such as Solite), for the inclusion of "sintering to bring to shipping grade and form, and loading for shipment."

The District Court found that the rotary kiln process applied by the petitioner here is a sintering process.

But the District Court held and the Court of Appeals affirmed that the petitioner's mineral is not one which is customarily sold in the form of a crude mineral product. The Courts' only reason for this holding ap-

pears to be that during the heating process changes occur in the mineral, equating "crude mineral product" with the raw mineral as it exists when removed from the mine, i.e., at the end of the purely extractive processes. In its opinion, the District Court stated that a standard handbook entitled "Industrial Minerals and Rocks" classifies lightweight aggregate as a crude mineral product but the Court rejects this classification because the handbook refers to it as a "manufactured" lightweight aggregate. But the handbook reference to "manufactured" is not intended to be a construction of the income tax laws and clearly was intended only to distinguish those lightweight aggregates which occur naturally from those which do not.

The petitioner's lightweight aggregate is not used as an end product but rather as a component (in the ordinary parlance of a manufacturer, a raw material) for the purpose of making other products. The evidence shows that there are numerous aggregates, including lightweight aggregates, which occur in nature and are used for the same purposes as petitioner's product. Manifestly, if sand, gravel and the other naturally occurring aggregates are crude mineral products (and, under the statute, "crude" cannot mean "raw" or "naturally occurring"), then the petitioner's lightweight aggregate is also a crude mineral product.

If the term "crude mineral product" means the mineral in the form in which it emerges from the mine, as the respondent contends, and if the application of a sintering process would cause the mineral to cease to be in the form of a crude mineral product, as the Courts below appear to have concluded, then Section 613(c)(4)(C) makes no sense whatever. This section provides that in

the case of minerals which are customarily sold in the form of a crude mineral product, sintering is an allowable process which may be applied to obtain a commercially marketable product. Yet the respondent has argued, and the Courts below seem to have held, that the application of a sintering process would cause any mineral to cease to be in the form of a crude mineral product. If that were the case, it could not be customarily sold in that form. Surely Congress did not intend to include a class of minerals and then provide for a process which in itself would prevent any mineral from falling within that class.

In the context of Section 613(c)(4)(C), the respondent's argument on this point cannot stand, and the holding of the Courts below is clearly wrong.

The District Court also held that the petitioner's sintering is not for the purpose of bringing the mineral to shipping grade and form. As to this we believe the Court was also wrong. We have been unable to find any authoritative definition of the term "shipping grade and form" but it has been held that the term "grade" is universally understood as refetring to quality. *Consolidated Water Power & Paper Co.* v. *Bowles,* 146 F. 2d 492 (1944). If the term "shipping grade" has any meaning at all, it must mean that grade or quality which can be shipped to market, i.e., a grade which is salable. If there is no market for weathered slate in its natural or raw state, how can it be said that it is then of shipping grade and form? How could the ordinary miner of weathered slate, to use the words of this Court in *Monolith,* have reached the point "where [he] shipped the product of his mine?" Clearly, by the use of these words, Congress intended to permit a miner to do such sintering as may

be necessary to improve the quality or grade of the mineral to the point that it is salable. Otherwise, the miner would not be permitted to process the mineral for which there is no market in order to obtain a commercially marketable mineral product.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

/s/ T. Howard Spainhour
Attorney for Petitioner

CERTIFICATE OF SERVICE

I, T. Howard Spainhour, attorney for Solite Corporation and a member of the Bar of the Supreme Court of the United States, do hereby certify that, on the 19th day of June, 1967, I served copies of the foregoing petition for writ of certiorari to the United States Court of Appeals for the Fourth Circuit (and Appendices thereto) upon the United States by depositing copies thereof in a United States Post Office, in a sealed envelope, with first class postage prepaid, duly addressed to the following, as required by Supreme Court Rule 33:

Mitchell Rogovin
Assistant Attorney General
Department of Justice
Washington, D. C. 20530

Hon. Thurgood Marshall
Solicitor General of the United States
Department of Justice
Washington, D. C. 20425

C. Vernon Spratley, Jr.
United States Attorney
Norfolk, Virginia 23510

/s/ T. Howard Spainhour
T. Howard Spainhour
Attorney for Solite Corporation
515 Virginia National Bank Building
Norfolk, Virginia 23510

June 19, 1967.

APPENDIX A

IN THE

United States District Court

E. D. VIRGINIA,
NORFOLK DIVISION

Civil Action No. 4095

SOLITE CORPORATION,
Plaintiff,

v.

UNITED STATES OF AMERICA,
Defendant.

May 16, 1966

WALTER E. HOFFMAN, Chief Judge.

On December 23, 1957, this Court rendered judgment in favor of Southern Lightweight Aggregates Corporation v. United States of America, Civil Action No. 2266, 58—1 U.S.T.C. para. 9235, 1 A.F.T.R. (2d) 392, in an action for the recovery of federal income taxes for the plaintiff's taxable years ending March 31, 1951, 1952 and 1953. The United States did not perfect any appeal from this decision. Shortly thereafter the name of the plaintiff was changed from Southern Lightweight Aggregates Corporation to Solite Corporation, but in all other respects the plaintiff's process of "mining" and "ordinary treatment process" remains the same. The

material facts and issues involved in the present litigation are essentially the same although the evidence herein presented is more extensive.

The instant proceeding is for the recovery of federal income taxes and interest thereon, in the aggregate sum of $31,979.70, for the fiscal year ended March 31, 1958. Presumably the decision will affect years subsequent to 1958.

Since the 1957 decision there have been several cases decided by the United States Supreme Court,[1] the Court of Appeals for the Fourth Circuit,[2] and more recently, the Court of Appeals for the Eighth Circuit,[3] which command a more searching examination of the facts and law. Prior to *Cannelton* (1960), it was universally held that taxpayers were entitled to treat as "ordinary treatment processes", for the purpose of determining their gross income for "mining" and, *a fortiori*, their percentage depletion deductions, all of the treatment processes normally applied by the taxpayers in order to obtain the first mineral product which could be "commercially marketable". The latter term, "commercially marketable", had been uniformly interpreted to mean an actual sufficient market existing therefor.[4] In-

1. United States v. Cannelton Sewer Pipe Co., 364 U.S. 76, 80 S.Ct. 1581, 4 L.Ed.2d 1581 (1960); Riddell v. Monolith Portland Cement Co., 371 U.S. 537, 83 S.Ct. 378, 9 L.Ed.2d 492 (1963).
2. Virginia Greenstone Company v. United States, 308 F.2d 669 (4 Cir., 1962).
3. United States v. Light Aggregates, Inc., 343 F.2d 429 (8 Cir., 1965).
4. United States v. Cherokee Brick and Tile Co., 218 F.2d 424 (5 Cir., 1955); Hitchcock Corp. v. Townsend, 232 F.2d 444 (4 Cir., 1956); United States v. Sapulpa Brick and Tile Corp., 239 F.2d 694 (10 Cir., 1956); United States v. Merry Brothers Brick and Tile Co., 242 F.2d 708 (5 Cir., 1957), cert. den. 355 U.S. 824, 78 S.Ct. 31, 2 L.Ed.2d 38; Dragon Cement Co. v. United States, 244 F.2d 513 (1 Cir., 1957), cert. den. 355 U.S. 833, 78 S.Ct. 50, 2 L.Ed.2d 45.

deed, two cases required "marketability at a profit".[5] Thus there was ample authority to support the 1957 decision of this Court in the action between the same parties but, of course, the prior conclusion cannot operate as an estoppel against the Government in the present case. As the Fourth Circuit pointed out in *Virginia Greenstone,* there is no need to be concerned with pre-*Cannelton* cases which may seem to point the other way.

Most of the essential facts have been the subject of a stipulation and, eliminating the formalities required as to filing a claim for refund, etc., we observe that the plaintiff-taxpayer, a Virginia corporation operating on a fiscal year basis ending March 31, is engaged in the business of extracting from the ground in Buckingham County, Virginia, a weathered material, commonly referred to as "weathered slate". The following steps are processes applied:

Step 1—The overburden, consisting of topsoil, on the surface of the ground is first removed.

Step 2—The weathered material lying below the top soil is then drilled and blasted and loaded on trucks, which carry said material to plaintiff's plant located approximately one-half mile from the quarry.

Step 3—The material is dumped from the trucks into the primary crusher and screener, where it is crushed and screened and then conveyed by a conveyor belt to a stock pile, from which it is conveyed by a conveyor belt and bucket elevator to a rotary kiln.

5. Commissioner v. Iowa Limestone Co., 269 F.2d 398 (8 Cir., 1959); Bookwalter v. Centropolis Crusher Co., 272 F.2d 391 (8 Cir., 1959).

Step 4—The material is fed into the high end of the rotary kiln (which is on an inclined axis) and, as the kiln turns, the material passes slowly from the higher end to the lower end of the kiln, from which heat is blown into the kiln.

Step 5—The material drops from the lower end of the kiln to the ground, where it stays long enough to become cool.

Step 6—The material is then placed, through the use of a clam shell bucket and crane, in the secondary crusher and screener, where it is crushed and screened and then loaded by a conveyor belt into freight cars.

It is conceded that no other substance or material of any kind is added during the above described treatment process. The rotary kiln is a "sintering process" which causes an agglomeration of the raw material by incipient fusion. The heat, approaching 2400°, causes the material to expand or bloat. In its final form taxpayer's product, sold under the tradename of "Solite", is used as a lightweight aggregate in making building units such as blocks.

Taxpayer contends that the finished lightweight aggregate as it emerges from the secondary crusher or, if not, then from the rotary kiln, is the first and only "commercially marketable mineral product" taken from its mining property, and that the rotary kiln process is an "ordinary treatment process" normally applied by mine owners to obtain the commercially marketable product. The Government urges that the cut-off point to "mining" is through the primary crusher stage of processing, i.e., at the end of Step 3. Because of the re-

cent decisions, especially the Eighth Circuit opinion in *Light Aggregates,* the Court agrees with the Government.

The pertinent statute involved is § 613 of the Internal Revenue Code of 1954 dealing with "Percentage Depletion". In substance it provides that in case of "mines and other natural deposits" the allowance for depreciation shall be the percentage of the gross income from the property.[6] The term "gross income from the property" is defined to mean "the gross income from mining". §613(c)(1). "Mining" is defined under §613(c)(2) as follows:

> "The term 'mining' includes not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products, and so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto as is not in excess of 50 miles unless the Secretary or his delegate finds that the physical and other requirements are such that the ore or mineral must be transported a greater distance to such plants or mills."

6. The percentage, as applied to the facts of this case and subject to the views expressed herein, is agreed to be 5% as the material when used by the mine owner was for use of "concrete aggregates, or for similar purposes." §613(b)(6).

Under § 613(c) (4) the term "ordinary treatment processes" is said to include—

> "(C) in the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering to bring to shipping grade and form, and loading for shipment;
>
> "(D) in the case of lead, zinc * * *; [and]
>
> "(E) the pulverization of talc, the burning of magnesite, and the sintering and nodulizing of phosphate rock."

From the foregoing it appears that the pertinent inquiries are (1) was the process adopted by the taxpayer in subjecting the material to the heat of the rotary kiln an "ordinary treatment process", (2) if so, was it applied to obtain the "commercially marketable mineral product", and (3) does the "sintering" process so applied constitute a requisite mining process involving a mineral "customarily sold in the form of a crude mineral product" or for the purpose of bringing the material "to shipping grade and form, and loading for shipment".

We must discount taxpayer's contention that the "sintering process" affords any comfort to the position advanced by plaintiff. Clearly the evidence shows that the lightweight aggregate is no longer customarily sold as a "crude mineral product" after it emerges from the rotary kiln; nor is the "sintering" for the purpose of bringing the material "to shipping grade and form, and loading for shipment". While an analysis of the components of the raw material taken from the Brenio Bluff quarry and the clinker emanating from the kiln are sub-

stantially identical, the X ray diffraction demonstrates a marked or radical chemical change or, as sometimes described, a compound change.[7]

The record adequately supports the taxpayer's argument that there were no actual sales of the unprocessed material by the plaintiff-taxpayer to others. In that sense there was certainly no "available market" as the layman would interpret the words, until the product emerges from the kiln. There is some intimation that the unprocessed material might be used "if you did not have anything better", or it could conceivably be used on "unimportant roads" but could not be sold in any quantity. There is a suggestion that it might be used as a roofing granule in conjunction with other products, although this contention is seriously disputed. Manifestly, it is too soft and without sufficient strength to meet any minimum specification in road work. In short, unless used for processing in the final production of lightweight aggregate, it is universally discarded. It serves no utility in industry prior to its introduction into the rotary kiln.

The difficulty with this argument is that the Supreme Court has unequivocally held and established that actual sales are not a prerequisite to commercial marketability. In *Cannelton,* the Court said:

> "Ever since the first percentage depletion statute, the cut-off point where 'gross income from mining' stopped has been the same, i.e., where the ordinary miner shipped the product of his mine, * * * [a]s

7. A standard handbook entitled "Industrial Minerals and Rocks" classifies lightweight aggregate as a "crude mineral product", but the passage from this handbook likewise indicates that it is a "manufactured" lightweight aggregate. For this reason the reference material is of little assistance in solving the issues presented.

we see it, the miner-manufacturer is but selling to himself the crude mineral that he mines, insofar as the depletion allowance is concerned."

Later, in United States v. Longhorn Portland Cement Company, 328 F.2d 491 (5 Cir., 1964), the Fifth Circuit, after discussing the effect of *Cannelton* and *Riddell,* pointed out that the allowance for depletion was limited to "the constructive income received from such crushed limestone"; and that Congress intended to grant miners a depletion allowance on constructive income from the raw material produced, if marketable in that form, and not on the value of the finished product.

It is, of course, argued that the cut-off point should be where the mineral became commercially marketable but, under the teachings of *Cannelton, Longhorn Portland Cement,* and *Light Aggregates,* we find that the true test of the cut-off is *where the mineral first became suitable for industrial use or consumption,* and this is to be treated as though the miner sold the material to himself for processing.

We need not enter into an extended discussion of taxpayer's status as an integrated mining operator. In the testimony of A. G. Ford, Director of Sales, Southern Lightweight Aggregate Corporation (plaintiff's predecessor name), before the Senate Committee on Finance in 1951, repeated references are made to the "manufacture" of lightweight aggregate. We think that the taxpayer's status reaches the point of being an integrated miner-manufacturer when the material reaches the rotary kiln.

The case of United States v. Light Aggregates, Inc., supra, is on all fours with the factual situation here pre-

sented. It involves the same finished product although the components of the raw material may be somewhat different. The material has the same expanding or bloating propensity when subjected to high temperatures. When the material emerges from the rotary kiln, it resembles a "clinker" such as in the case under consideration. We find this Eighth Circuit opinion to be controlling in all respects and accordingly must dismiss the complaint herein.

A judgment order will be entered upon presentation and endorsement by counsel. No attempt has been made to compute the correctness of the tax collected and is only intended to determine the factual and legal issues governing the assessment of said tax.

APPENDIX B

United States Court of Appeals

FOR THE FOURTH CIRCUIT

No. 10,861

SOLITE CORPORATION,

Appellant,

versus

UNITED STATES OF AMERICA,

Appellee.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF VIRGINIA, AT NORFOLK. WALTER E. HOFFMAN, DISTRICT JUDGE.

(Argued February 7, 1967. Decided March 30, 1967.)

Before HAYNSWORTH, Chief Judge, and J. SPENCER BELL and CRAVEN, Circuit Judges.

J. SPENCER BELL, Circuit Judge:

This is an appeal by the plaintiff taxpayer from an adverse judgment of the district court in a suit to recover alleged overpayments of federal income tax for 1958.

The taxpayer, a Virginia corporation, is engaged in the production of a lightweight aggregate used in the manufacture of building blocks and other building units. The lightweight aggregate, known by the trade name "Solite," is produced from a weathered material mined

by the taxpayer. The processes employed by the taxpayer, some of which are patented, were stipulated by the parties as follows:

"(a) The overburden, consisting of top soil on the surface of the ground, is first removed.

"(b) The weathered material lying below the top soil is then drilled and blasted and loaded on trucks, which carry said material to the plaintiff's plant located a short distance (approximately one-half mile) from the quarry.

"(c) The material is dumped from the trucks into the primary crusher and screener, where it is crushed and screened and then conveyed by a conveyor belt to a stock pile, from which it is conveyed by a conveyor belt and bucket elevator to a rotary kiln.

"(d) The material is fed into the high end of the rotary kiln (which is on an inclined axis) and as the kiln turns the material passes slowly from the higher end of the lower kiln, from which heat is blown into the kiln.

"(e) The material drops from the lower end of the kiln to the ground, where it stays long enough to become cool.

"(f) The material is then placed, through the use of a clam shell bucket and crane, in the secondary crusher and screener, where it is crushed and screened and then loaded by a conveyor belt into freight cars."

It was also stipulated that no other material of any kind is added during the processing and that the taxpayer

sells all of the processed material and does not use any of it in the manufacture of any other product.

The parties agree that the taxpayer is entitled to a five per cent depletion allowance under section 613 of the Internal Revenue Code of 1954.[1] The Government contends, however, that the taxpayer is entitled to a depletion allowance only on that portion of its gross income attributable to steps (a) through (c) of the processing set out above. The taxpayer, on the other hand, argues that it is entitled to a percentage depletion allowance on its entire gross income from the sale of the lightweight aggregate after all processing, or at least through step (d) (the kiln process). The district court held that only the gross income from the first three steps ((a) through (c)) of the processing could be considered in determining the amount of the taxpayer's depletion allowance, and we affirm.

The depletion allowance provided by section 613 is the allowable percentage "of the gross income from the property." 26 U.S.C.A. §613(a). The term, "gross income from the property," is defined in subsection 613(c)(1) as "the gross income from mining," and the term "mining" is defined in subsection 613(c)(2) as including "not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products . . ."[2] The question for considera-

1. Because the instant proceeding is for the recovery of overpayments for the fiscal year which ended March 31, 1958, we are not concerned with the amendments to the statute which have become effective after that date.

2. The wording of 26 U.S.C.A. §613(c)(2) was substantially changed by a 1960 amendment.

tion on appeal is to what extent plaintiff taxpayer's processes are "ordinary treatment processes" within the meaning of the statute.

Subsection 613(c)(4) specifies certain processes which will be considered mining under the statute, and the taxpayer contends that its kiln process is specifically included in that subsection:

> "(4) *Ordinary treatment processes.*—The term "ordinary treatment processes" includes the following:
>
> . . .
>
> (C) in the case of . . . minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering to bring to shipping grade and form, and loading for shipment; . . . "

The district court found that the lightweight aggregate is not "customarily sold in the form of a crude mineral product" after the kiln process (established by the record to be a "sintering" process), and that the sintering is not for the purpose of bringing the material "to shipping grade and form." The district court's findings are adequately supported by the record and are not clearly erroneous.

The construction of "ordinary treatment processes normally applied . . . to obtain the commercially marketable mineral product or products" was recently considered by the United States Supreme Court in *United States* v. *Cannelton Sewer Pipe Co.*, 364 U.S. 76 (1960). In that case the Court made it clear that percentage depletion cannot be used to give an advantage to the inte-

grated miner-manufacturer which is not shared by non-integrated miners and manufacturers. The taxpayer in the case at bar contends that it is not an integrated miner-manufacturer but a miner only, that it sells its product when it first becomes "commercially marketable," and that prior to the kiln process, the weathered material, which is a soft slate, is worthless. The district court found that there was no actual market for the taxpayer's mineral before the kiln process and that "unless used for processing in the final production of lightweight aggregate, it is universally discarded." The *Cannelton* case established that actual sales by the taxpayer are not required in order for a mineral to be classified as "commercially marketable." The Court in *Cannelton* also stressed that depletion is not allowed for processes designed to give a mineral worth "but for exhaustion of mineral assets alone." *Id.* at 88. The Court stated that if the mineral is worthless there can be no depletion: "One cannot deplete nothing." *Ibid.*

Neither is it determinative that the taxpayer is apparently the only producer in the United States of lightweight aggregate from this particular material, with the result that there are virtually no sales of the material anywhere before it is processed in a kiln, since the material has no use other than in the production of lightweight aggregates. In *Virginia Greenstone Co.* v. *United States,* 308 F.2d 669 (4 Cir. 1962), this court held that although the taxpayer in that case had a monopoly on greenstone, in that it controlled the only source of supply, it could not contend that the first "commercially marketable" product was its finished stones, since other dimension stone with which the taxpayer completed was in fact sold before the finishing process. The taxpayer in the

instant case does not have a monopoly of the supply of soft slate, but we do not think the existence of such a monopoly is essential to the principle established by the *Virginia Greenstone* case. The record in the case at bar indicates that there are manufacturers of lightweight aggregates processed from various other minerals which compete with the taxpayer's product, and some of them at least purchase the material used in their production rather than mine it themselves. If there are miners of materials used in the production of lightweight aggregates who sell that material before employing the kiln process, then surely miners who themselves employ the kiln process are miner-manufacturers within the meaning of the *Cannelton* case. It is obvious that the construction of the percentage depletion allowance statute contended for by the taxpayer would give it "a decided competitive advantage over its nonintegrated manufacturer competitor. Congress never intended that depletion create such a discriminatory situation. As we see it, the miner-manufacturer is but selling to himself the crude mineral that he mines, insofar as the depletion allowance is concerned." *United States* v. *Cannelton Sewer Pipe Co.*, 364 U.S. at 87.

We do not interpret the cases as requiring that a market be actually available to the taxpayer in order for its mineral to be "commercially marketable" within the meaning of the statute. In *Riddell* v. *Monolith Portland Cement Co.*, 371 U.S. 537, 538 (1963), the Court pointed out that it had held in the *Cannelton* case that "the statutory percentage depletion allowance on the gross income of an integrated mining operator should be cut off at the point where the mineral first became suitable for industrial use or consumption." Since the material mined by

the taxpayer is physically susceptible of being transported, although transporting it over a considerable distance may not be economically feasible, and since others in the same industry purchase similar mateirals for use in the manufacture of a product substantially the same as the taxpayer's, we conclude that the mineral is "suitable for industrial use or consumption."

The taxpayer points out that in the *Cannelton* and *Monolith Portland Cement Co.* cases there was evidence of "substantial" markets for the minerals there involved. We do not think, however, that a finding of "substantial" sales of the material when it first becomes "suitable for industrial use or consumption" is an essential requirement of the result in those cases. The Eighth Circuit, in *United States* v. *Light Aggregates, Inc.,* 343 F.2d 429 (8 Cir. 1965), reached the same result even though only three per cent of the total national production of clays and shales, the minerals there in question, were sold by producers in their raw state, and none of those sales were in the taxpayer's state. In that case, as in the case at bar, the taxpayer, a producer of a lightweight aggregate, was attempting to compute its depletion allowance on the basis of the gross income from the sale of its lightweight aggregate after the kiln process. The court held that the kiln process was a manufacturing and not a mining process.

The judgment of the district court is

Affirmed.

APPENDIX C

§611. ALLOWANCE OF DEDUCTION FOR DEPLETION

(a) General rule.—In the case of mines, oil and gas wells, other natural deposits, and timber, there shall be allowed as a deduction in computing taxable income a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under regulations prescribed by the Secretary or his delegate. For purposes of this part, the term "mines" includes deposits of waste or residue, the extraction of ores or minerals from which is treated as mining under section 613 (c). In any case in which it is ascertained as a result of operations or of development work that the recoverable units are greater or less than the prior estimate thereof, then such prior estimate (but not the basis for depletion) shall be revised and the allowance under this section for subsequent taxable years shall be based on such revised estimate.

(b) Special rules.—

(1) Leases.—In the case of a lease, the deduction under this section shall be equitably apportioned between the lessor and lessee.

(2) Life tenant and remainderman. — In the case of property held by one person for life with remainder to another person, the deduction under this section shall be computed as if the life tenant were the absolute owner of the property and shall be allowed to the life tenant.

(3) Property held in trust.—In the case of property held in trust, the deduction under this section shall be apportioned between the income beneficiaries and the trustee in accordance with the pertinent provisions of the instrument creating the trust, or, in the absence of such provisions, on the basis of the trust income allocable to each.

(4) Property held by estate.—In the case of an estate, the deduction under this section shall be apportioned between the estate and the heirs, legatees, and devisees on the basis of the income of the estate allocable to each.

(c) Cross reference.—

For other rules applicable to depreciation of improvements, see section 167.

§613. PERCENTAGE DEPLETION

(a) General rule.—In the case of the mines, wells, and other natural deposits listed in subsection (b), the allowance for depletion under section 611 shall be the percentage, specified in subsection (b), of the gross income from the property excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property. Such allowance shall not exceed 50 per cent of the taxpayer's taxable income from the property (computed without allowance for depletion). In no case shall the allowance for depletion under section 611 be less than it would be if computed without reference to this section.

(b) Percentage depletion rates.—The mines, wells,

and other natural deposits, and the percentages, referred to in subsection (a) are as follows:

(1) 27½ per cent—oil and gas wells.

(2) 23 per cent—

(A) sulfur and uranium; and

(B) if from deposits in the United States —anorthosite (to the extent that alumina and aluminum compounds are extracted therefrom), asbestos, bauxite, beryl, celestite, chromite, corundum, fluorspar, graphite, ilmenite, kyanite, mica, olivine, quartz crystals (radio grade), rutile, block steatite talc, and zircon, and ores of the following metals: antimony, bismuth, cadmium, cobalt, columbium, lead, lithium, manganese, mercury, nickel, platinum and platinum group metals, tantalum, thorium, tin, titanium, tungsten, vanadium, and zinc.

(3) 15 per cent—ball clay, bentonite, china clay, sagger clay, metal mines (if paragraph (2) (B) does not apply), rock asphalt, and vermiculite.

(4) 10 per cent—asbestos (if paragraph (2) (B) does not apply), brucite, coal, lignite, perlite, sodium chloride, and wollastonite.

(5) 5 per cent—

(A) brick and tile clay, gravel, mollusk shells (including clam shells and oyster shells), peat, pumice, sand, scoria, shale, and stone, except stone described in paragraph (6); and

(B) if from brine wells—bromine, calcium chloride, and magnesium chloride.

(6) 15 per cent—all other minerals (including, but not limited to aplite, barite, borax, calcium carbonates, refractory and fire clay, diatomaceous earth, dolomite, feldspar, fullers earth, garnet, gilsonite, granite, limestone, magnesite, magnesium carbonates, marble, phosphate rock, potash, quartzite, slate, soapstone, stone (used or sold for use by the mine owner or operator as dimension stone or ornamental stone), thenardite, tripoli, trona, and (if paragraph (2) (B) does not apply) bauxite, beryl, flake graphite, fluorspar, lepidolite, mica, spodumene, and talc, (including pyrophyllite), except that, unless sold on bid in direct competition with a bona fide bid to sell a mineral listed in paragraph (3), the percentage shall be 5 per cent for any such other mineral when used, or sold for use, by the mine owner or operator as riprap, ballast, road material, rubble, concrete aggregates, or for similar purposes. For purposes of this paragraph, the term "all other minerals" does not include—

(A) soil, sod, dirt, turf, water, or mosses; or

(B) minerals from sea water, the air or similar inexhaustible sources.

(c) Definition of gross income from property.—For purposes of this section—

(1) Gross income from the property. — The term "gross income from the property" means, in the case of a property other than an oil or gas well, the gross income from mining.

(2) Mining.—The term "mining" includes not merely the extraction of the ores or minerals from

the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products, and so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto as is not in excess of 50 miles unless the Secretary or his delegate finds that the physical and other requirements are such that the ore or mineral must be transported a greater distance to such plants or mills.

(3) Extraction of the ores or minerals from the ground.—The term "extraction of the ores or minerals from the ground" includes the extraction by mine owners or operators of ores or minerals from the waste or residue of prior mining. The preceding sentence shall not apply to any such extraction of the mineral or ore by a purchaser of such waste or residue or of the rights to extract ores or minerals therefrom.

(4) Ordinary treatment processes.—The term "ordinary treatment processes" includes the following:

(A) In the case of coal—cleaning, breaking, sizing, dust allaying, treating to prevent freezing, and loading for shipment;

(B) in the case of sulfur recovered by the Frasch process — pumping to vats, cooling, breaking, and loading for shipment;

(C) in the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals

which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering to bring to shipping grade and form, and loading for shipment;

(D) in the case of lead, zinc, copper, gold, silver, or fluorspar ores, potash, and ores which are not customarily sold in the form of the crude mineral product — crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, crystallization, precipitation (but not including as an ordinary treatment process electrolytic deposition, roasting, thermal or electric smelting, or refining), or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore, including the furnacing of quicksilver ores; and

(E) the pulverization of talc, the burning of magnesite, and the sintering and nodulizing of phosphate rock.

(d) Application of percentage depletion rates to certain taxable years ending in 1954.—

(1) General rule.—At the election of the taxpayer in respect of any property (within the meaning of the Internal Revenue Code of 1939), the percentage specified in subsection (b) in the case of any mine, well, or other natural deposit listed in such subsection shall apply to a taxable year ending after December 31, 1953, to which the Internal Revenue Code of 1939 applies.

(2) Method of computation. — The allowance for depletion, in respect of any property for which an election is made under paragraph (1) for any taxable year, shall be an amount equal to the sum of—

(A) that portion of a tentative allowance, computed under the Internal Revenue Code of 1939 without regard to paragraph (1) of this subsection, which the number of days in such taxable year before January 1, 1954, bears to the total number of days in such taxable year; plus

(B) that portion of a tentative allowance, computed under the Internal Revenue Code of 1939 (as modified solely by the application of paragraph (1) of this subsection), which the number of days in such taxable year after December 31, 1953, bears to the total number of days in such taxable year.

In the Supreme Court of the United States

OCTOBER TERM, 1967

No. 269

SOLITE CORPORATION, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

The question here is what constitutes petitioner's "gross income from mining", which is its base for the percentage depletion allowance under Section 613 of the Internal Revenue Code of 1954. In this case the controversy is controlled by a determination of the point at which the operation of petitioner's business ceases to be "mining," which Section 613(c)(2) defines to include "ordinary treatment processes * * * applied * * * in order to obtain the commercially marketable mineral product or products * * *."

Petitioner extracts weathered soft slate from the ground, crushes it, and converts the crushed slate into a lightweight aggregate by a kiln process which

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causes bloating and chemical changes. Petitioner then crushes the aggregate and sells it under the trade name "Solite" for use in the manufacture of building blocks and the like. Petitioner contends that its kiln process is a mining "treatment process" within the purview of Section 613(c)(2), and hence that its gross sales receipts less only the income attributable to crushing the aggregate constitute its depletable "gross income from mining". The district court and the court below rejected this contention, holding that petitioner's mining processes terminated prior to the kiln process.

This ruling is a correct application of criteria established by this Court in *United States* v. *Cannelton Sewer Pipe Co.*, 364 U.S. 76, and *Riddell* v. *Monolith Cement Co.*, 371 U.S. 537. There is neither a conflict in decisions nor any other appropriate ground for further review by this Court.

1. Petitioner's primary contention is that its post-kiln lightweight aggregate is its first "commercially marketable mineral product" within the meaning of Section 613(c)(2); that the crushed weathered soft slate is not "commercially marketable" in the statutory sense because there is no evidence of actual sales of the material in this form. This contention is unsound.

This Court has made clear that actual sales of, or markets for, a raw mineral material are not prerequisites of commercial marketability. A mineral is deemed "commercially marketable" for depletion purposes "at the point where the mineral first became suitable for industrial use or consumption". *Riddell* v. *Monolith*

Cement Co., supra at 538. Evidence of actual sales is one form of "conclusive proof" that a mineral is "ready for industrial use or consumption", *United States* v. *Cannelton Sewer Pipe Co., supra* at 86; but the absence of such sales or a readily available market does not require the converse conclusion.

A process that physically and chemically transforms a raw mineral into a new and more valuable product is a manufacturing process, not a mining process, albeit employed by integrated miner-manufacturers who do not buy and sell the raw material. When a mineral is ready for manufacturing processes and in shipping form, so that it could be delivered to any manufacturer making the same product, it is ready and suitable for industrial use or consumption, and therefore "commercially marketable" within the meaning of Section 613(c)(2). The absence of a market where sales of the raw material may be made at a profit is immaterial. The integrated miner-manufacturer is deemed to be his own market or customer and his depletion basis is limited to the constructive income from the raw mineral in shipping form—the raw fire clay and shale in *Cannelton,* the crushed limestone in *Monolith,* and the crushed slate in the case at bar. Accord, *United States* v. *Longhorn Portland Cement Co.,* 328 F. 2d 491 (C.A. 5); *Virginia Greenstone Co.* v. *United States,* 308 F. 2d

669 (C.A. 4); *United States* v. *Light Aggregates, Inc.*, 343 F. 2d 429 (C.A. 8).[1]

In the instant case the record shows, and the court below found, that petitioner's crushed slate was ready for delivery to and consumption by its competitors in the manufacture of lightweight aggregate (R. 44a, 53a; Supp. R. 108–109).[2] Moreover, some of petitioner's competitors purchase their minerals in pre-kiln form rather than mine it themselves (Pet. 16a).[3] And petitioner itself leases some quarries and pays royalties for the raw mineral extracted (Supp. R. 111–112, 130–131). Thus, in the light of the applicable criteria, the record amply warrants the ruling of the court below that petitioner's crushed slate

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[1] In *Monolith* the Ninth Circuit had ruled in favor of the taxpayer (an integrated miner-manufacturer of cement) on precisely the same ground petitioner urges here, that the absence of an actual market for the taxpayer's raw mineral distinguished the case from *Cannelton* and required the conclusion the raw material was not "commercially marketable". 301 F. 2d 488. In reversing, this Court did not deem the matter of actual sales sufficiently important to discuss in the text of its opinion, merely observing in a footnote that there were sales of crushed limestone for purposes other than the manufacture of cement. (371 U.S. 539.)

[2] "R." refers to the appendix to the brief for the Appellant filed in the court of appeals; "Supp. R." refers to Appendix B to the brief for appellee filed in that court.

[3] Petitioner is the only producer of lightweight aggregate using weathered soft slate as the raw material; its competitors use clay, shale and other types of slate which are also used by petitioner's subsidiaries (R. 28a–32a). But lightweight aggregate is essentially the same product of the same process, whatever the raw material. Lightweight aggregate is made by a heating process referred to as incipient fusion, here effected through the use of the rotary kiln (R. 33a). The only difference between the product made from clay and that made from slate is in color (R. 29a).

was the "commercially marketable" end-product of petitioner's mining processes.

2. Petitioner also contends that its kiln process is a "sintering" process[4] within the meaning and context of Section 613(c)(4)(C), which, "in the case of * * * minerals which are customarily sold in form of a crude mineral product" provides that mining processes include "sorting, concentrating, and sintering to bring to shipping grade and form * * *."

Kiln processes are a form of "sintering". However, it is clear on the face of the statute that "sintering to bring to shipping grade and form" refers back to customary sales of crude minerals, and contemplates only those "sintering" processes which ready the crude mineral for shipment and manufacture, *i.e.*, make it "suitable for industrial use or consumption" in the language of *Monolith. United States* v. *Cannelton Sewer Pipe Co., supra* at 84–86; *United States* v. *Longhorn Portland Cement Co., supra* at 496.

As the District Court found, petitioner's kiln process is *not* the sort of sintering process described in Section 613(c)(4)(C), but rather is a manufacturing process which comes after the material is suitable for sale and transforms the crude mineral, both physically and chemically,[5] into an entirely new prod-

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[4] "Sintering" generally refers to a heating process which, without melting, agglomerates fine otherwise unmanageable particles into a bloated coherent mass.

[5] "Sintering" may be used to agglomerate fine particles for shipping purposes without otherwise affecting the chemical or physical nature of the mineral, as in the case of powdered phosphate rock. See Hearings before the Senate Committee on Finance on the Internal Revenue Code of 1954, 83d Cong., 2d Sess., Pt. 3, pp. 1334–1338.

uct, *United States v. Cannelton Sewer Pipe Co., supra,* p. 86; *United States* v. *Light Aggregates, Inc., supra.*

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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AUGUST, 1967.

U.S. GOVERNMENT PRINTING OFFICE: 1967